Partnerships and legal personality

Partnerships and Legal Personality: Cautionary Tales from Scotland

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Abstract: This article analyses the separate legal personality of partnerships, drawing on Hansmann and Kraakman's identification of the attributes shared by businesses possessing legal personality. Their work provides a jurisdictionally-neutral standard of comparison which is applied here to the Scottish partnership which, unusually amongst jurisdictions influenced by the common law tradition, possesses separate legal personality. The historical development of Scottish partnerships is explored, from its origins as a Roman-inspired type of *societas*, a contract centred on the internal rights and duties of the partners *inter se,* towards a modern, outward-facing business able to contract with third parties in its own name. Challenging orthodoxy in Scottish scholarship, the author identifies the period during which Scots law moved from contractually-inspired partnership to partnership secured by organisational law, and specifically entity shielding. To this extent, Scots law supports Hansmann and Kraakman's view that attributes of legal personality develop gradually, and are secured by organisational law rather than contract law. Disagreeing with them, however, she uses the Scottish experience to illustrate that lack of perpetual succession is not, as they argue, a "mere inconvenience which can easily overcome with contractual workarounds", but rather an essential requirement of a workable partnership with legal personality.

Keywords: partnership law, legal personality, Scots law, legal history, entity theory

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Partnerships and Legal Personality: Cautionary Tales from Scotland

Laura Macgregor *

Introduction

This article analyses the separate legal personality of partnerships, drawing on published work by Hansmann and Kraakman in order to do so. Their identification of the attributes shared by businesses possessing legal personality provides a jurisdictionally-neutral standard of comparison available for use in order to assess national partnerships. It is applied here to the Scottish partnership which, unusually amongst jurisdictions which have been influenced by the common law tradition, possesses separate legal personality. The historical development of Scottish partnerships is explored, from its origins as a Roman-inspired type of *societas*, a contract centred on the internal rights and duties of the partners *inter se,* towards a modern, outward-facing business able to contract with third parties in its own name. This historical analysis lends support to Hansmann and Kraakman's ultimate thesis, which is that organisational law (and not contract law) provides the rules which are necessary to allow businesses to function efficiently. Challenging orthodoxy in Scottish scholarship, and drawing on new historical evidence, the author suggests that attributes of legal personality developed earlier than has been thought, in the late eighteenth rather than the early nineteenth century. At this point Scots law began to move from a contractually-inspired partnership to partnership secured by organisational law, and specifically entity shielding.

Whilst the Scottish experience broadly supports Hansmann and Kraakman's views, it nevertheless highlights an omission from their framework. They suggest that the lack of perpetual succession in a business is an "inconvenience", easily avoided by contractual workarounds.[1] The author uses modern Scots law to illustrates that contractual

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[1] H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale LJ 387 (hereinafter "Hansmann and Kraakman") 413, and, with R Squire, 'Law and the Rise of the Firm' (2006) 119 Harvard L Rev 1335 ("hereinafter Hansmann, Kraakman and Squire"). 1394.

workarounds are conceptually and practically flawed. More broadly, the Scottish experience shows that entity shielding, whilst undoubtedly the most significant factor in the efficient running of business, is not enough *in itself* to secure efficient businesses. Perpetual succession is also necessary because without it, the important benefits of entity shielding are rendered meaningless. Finally, it is to organisational law, and not contract law, that the author looks in order to reform modern Scots law.

Although engagement with Hansmann and Kraakman's thesis is important as an end in itself, there are other reasons why Scottish partnership law is of interest beyond Scotland. The most recent review of partnership law by the Law Commission and the Scottish Law Commission recommended the adoption of separate legal personality for all UK partnerships.[2] The Scottish experience reminds reformers that legal personality is only workable if bolstered by perpetual succession. By providing the first detailed analysis of Scottish legal personality, this article also fills a gap in knowledge, particularly useful for UK businesses involved in cross-border transactions. Finally, it is likely to be of interest to those involved in the private equity and venture capital context, where the separate legal personality of the Scottish limited partnership has led to its widespread use.[3]

Turning to the scheme of the article, in the first of three Sections the focus lies on the meaning of legal personality. It is suggested that entities show different defining attributes at different stages in their legal development. It is therefore a conclusory label: we must enquire behind the label to the general law in order to find out what it actually involves. Kraakman et al's views on the attributes of legal personality are summarised and then applied to Scottish partnerships. The problem of perpetual succession, described here as "continuity", is outlined. The second part contains, in essence, the historical exposition in which the stages of the development towards Scottish legal personality are identified. This section contains analysis of case law not previously discussed in published scholarship. Drawing on late eighteenth and early nineteenth century sources, the author challenges the prevailing view that legal personality was the creation of the institutional writer, George

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[2] Partnership Law, (Law Com No 283, Scot Law Com No 192), 10 October 2003.

[3] British Private Equity and Venture Capital Association Briefing, "The Importance of UK Limited Partnerships for Private Equity & Venture Capital", 3, available at: https://www.bvca.co.uk/LinkClick.aspx?fileticket=dWRGpm3xElY%3D&portalid=0&timestamp=1534942822184.

Joseph Bell. The third part analyses more deeply the problem of lack of continuity in Scots law, illustrating why contractual workarounds do not provide an adequate solution.

Section 1. Attributes Shared by Businesses Having Legal Personality

A. The Goal of the Search

Before embarking on a search for legal personality, it is useful to reflect on what we are actually looking for. Susan Reynolds, writing about corporations, stated:

> "Legal concepts are not like thimbles, to be found in inappropriate places. They exist only within appropriate legal systems. The concept of a legal corporation, a legal personality, can exist only within a system in which there are things which an individual or a corporate group can do and suffer which an unincorporated group cannot. It also needs circumstances in which people feel a fairly serious need to distinguish the responsibilities of individuals from those of the groups to which they belong."[4]

This focusses our attention on practical activities of groups of people taking place in a legal context.

Hunter, discussing the personality of the Scottish Burgh, counselled against treating the historical development as though it were "…a gradual but inevitable process of jurisprudential enlightenment".[5] There is unlikely to be a 'finish line' to the race of achieving legal personality. In other words, we are unlikely to find a uniform idea of legal personality which applies to all partnerships, only the attainment (in varying degrees) of different attributes of legal personality.

Manifestations of the ability to act as a group might include the ability to conclude contracts in the name of the group, to sue and be sued in that name, or to own property in that name. The group will have an identity distinct from the identity of the individuals who comprise it. This difference of identity gives it continuity, leaving the firm unaffected by events which impact upon the members themselves. In other words, the firm should

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[4] S Reynolds, The Idea of the Corporation in Western Christendom before 1300, in J A Guy and H G Beale (eds), *Law and Social Change in British History* (1984) 27 at 28.
[5] R L C Hunter, "Corporate Personality and the Scottish Burgh" in G W S Barrow (ed), *The Scottish Tradition Essays in honour of Ronald Gordon Cant* (1974) 223 at 223.

continue when members leave the group through retiral or death, or join the group through assumption.

B. Kraakman et al's Framework of Legal Personality

Although the particular focus of the work of Kraakman et al is company law, their language, especially "organizational forms" takes in other types of business (including the partnership). Legal personality is, to them, not a highly significant idea, but rather a "convenient heuristic formula", which "…is not in itself an attribute that is a necessary precondition for the existence of any – or indeed all - of these rules, but merely a handy label for a package that conveniently bundles them together".[6]

They suggest that legal personality is a term which can be applied to organisational forms which share three attributes.[7] The first is the ability to operate as a single contracting party, separately from the individuals who own and manage the firm.[8] The firm is described by them as a "nexus for contracts".[9] Drawing on civilian ideas of a separate patrimony, they identify the importance of the pool of assets owned by the firm which is distinct from the assets of the owners of the firm.[10] This separate pool of assets facilitates the firm's contracts by providing third parties with reassurance that the firm will perform its contractual obligations. The firm can "bond" its contracts, offering satisfaction for the firm's obligations through the "bonding assets".[11] This process, which they describe as "entity shielding",[12] involves two separate ideas. The first is the claim which the firm's creditors have to the firm's assets which is prior to the claim which the owners' personal creditors have to the assets of the firm. They specifically note that this rule is something which corporate law shares with partnership law.[13] The assets are available for the enforcement of

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[6] Kraakman et al, 8.
[7] Reinier Kraakman, John Armour, Paul Davies, Luca Enriques, Henry Hansmann, Gerard Hertig, Klaus Hopt, Hideki Kanda, Mariana Pargendler, Wolf-Georg Ringe, and Edward Rock, *The Anatomy of Corporate Law,* 3rd edn, (2017) (hereinafter "Kraakman et al") 8.
[8] Ibid, 5.
[9] Ibid.
[10] See the reference to civilian ideas of separate patrimony in Kraakman et al, 5.
[11] Hansmann and Kraakman, 392.
[12] See Hansmann and R Kraakman, and Hansmann, Kraakman and Squire.
[13] Kraakman et al, 6.

the firm's contractual liabilities, and, as a result, render the firm's contractual commitments "credible".[14] The second idea is a rule of "liquidation protection", which prevents the owners from withdrawing their capital from the firm at will, and prevents also the owners' personal creditors from foreclosing on the owner's share of firm assets.[15] If either of these were possible, it would result in liquidation of the firm.

Kraakman et al conclude that liquidation protection is found in corporations, but not in partnerships. Partnerships therefore have only "weak-form" entity shielding, in contrast to the strong form possessed by the company.[16] Strong form entity shielding facilitates tradability of the company's shares. Kraakman et al's first attribute is an extensive one, taking in not only the ability to contract but the way in which a business uses its assets to bond those contracts and the application of bankruptcy or insolvency law to firm assets.

Their second attribute focusses on the way in which the firm is managed, essentially expressing agency rules. There is a need to identify the actors who are authorised to enter into contracts, or buy and sell assets, on behalf of the firm. Their third attribute relates to the rules which are necessary to allow the firm to raise litigation in the name of the firm, or "suing in appellation".

C. Application of Kraakman et al's Framework to Scottish Partnership Law

Before applying Kraakman et al' framework to Scots law, it is worth noting that, in Scots law, all types of partnerships are treated as possessing legal personality: the general partnership; the Limited Partnership; and the Limited Liability Partnership.[17] Exactly why Scots law developed in such a different way to English law is an issue explored in Section 2.

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[14] Ibid.

[15] Ibid. Although "foreclose" is used in Scots law (see s 28, conveyancing and Feudal Reform (Scotland) Act 1970) it is not used in the same sense in which it is used by Hansmann and Kraakman. Parallels could be drawn in Scots law with the law of 'diligence': "an umbrella term for a range of debt recovery and enforcement processes as well as for the rights obtained as a result of those processes", Fraser Davidson, Denis J Garrity, Laura J Macgregor, Alisdair D J MacPherson and Lorna Richardson, *Commercial Law in Scotland,* 5th edn, (2018) para 8.1.

[16] Kraakman et al, 6.

[17] See Partnership Act 1890, s 4(2). The 1890 Act applies except as amended by the Limited Partnership Act 1907 in relation to limited partnerships. The Limited Liability Partnership Act 2000, s1(2) creates for the whole of the UK a body corporate with legal personality separate from that of its members.

Kraakman et al's first attribute was the ability of the firm to enter into contracts in its own name; an ability linked to ownership of assets.[18] A Scottish partnership (or firm)[19] can indeed enter into contracts in its own name. The position in relation to ownership of assets is more complicated and differs depending on the nature of the asset concerned. The firm may own moveable property, including for example intellectual property rights, in its own name. It was only in 2004, following statutory change, that the Scottish firm became able to hold title to land (or heritable property, using Scottish terminology) in its own name.[20] Prior to that date, title could be taken by the partners in their own names as trustees for the firm.[21] The latter practice continues, notwithstanding the statutory change.[22] The Scottish firm can enter into leases of heritable property in its own name.[23] It is, however, common for leases to be entered into by the firm *and* the partners as trustees for the firm.[24]

In summary, the Scottish firm does not use its ability to own assets in its own name to full effect. The practices described above, namely adding the partners as trustees, are indicative of concerns over the Scottish firm's legal personality. As we shall see shortly, such concerns relate to the Scottish firm's lack of perpetual succession.

Recalling, for the moment, the work of Kraakman et al, they suggest that the firm's ability to contract is facilitated by entity shielding. The firm can bond its contracts, offering satisfaction for the firm's obligations through these bonding assets. Entity shielding provides firm creditors with priority over the owners' creditors in relation to firm debts, and also provides liquidation protection, preventing the owners from withdrawing their capital at will. Applying these ideas to Scots law, where both the firm *and* the partners are

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[18] Kraakman et al, 6.

[19] In the Partnership Act 1890, s1 indicates that "partnership" should be applied to the actual relation between the partners, whereas s4 indicates that "firm" should be applied to the collective entity which is the partnership.

[20] Section 70, Abolition of Feudal Tenure etc (Scotland) Act 2000, which came into force on 28 November 2004.

[21] *Munro v Stein* 1961 SC 362.

[22] S Chan, *A Practical Guide To Partnership Law in Scotland* (2018) para 9-16.

[23] *Dennistoun Macnayr & Co v Macfarlane* (1808) Mor. App. Tack No 15. Gretton, writing in the late 80s, stated that leases are taken in the name of the firm "often (though not invariably)", 'Who owns partnership property?' (1987) Jur Rev 163 at 175.

[24] According to Reid and Gretton this approach makes "little sense". It involves both the trustees and the beneficiaries being contracting parties at the same time, K G C Reid and G L Gretton, *Conveyancing 2017* 48, discussing *Oag v Oag's Exrs* 2017 GWD 25-423, Land Ct. See also *Jardine-Paterson v Fraser* 1974 SLT 93, per Lord Maxwell at 94-95.

sequestrated, the firm's creditors have first claim on the assets of the firm.[25] Only once those creditors are paid in full do a partner's personal creditors have any claim on the firm's remaining assets.[26] The partner's personal creditors then have a claim against the partner's share in the firm (the latter being an incorporeal moveable right).[27] They would be able to arrest that partner's share in the firm, in the hands of the firm, having a freezing effect on the firm's assets.[28] If the partner is solvent, the partner's personal creditors have no claim over the firm's assets. Such a creditor could arrest the partner's share in the firm but could not force the liquidation of the firm's assets.

The extent of liquidation protection provided in Scottish partnerships depends upon whether the partnership is a partnership at will or a partnership of fixed duration. A partnership at will is of unlimited duration and can be dissolved easily, by giving notice to the other partners.[29] Thus one partner (and by proxy, the partner's personal creditors), can dissolve the firm and force a liquidation of the firm's assets.[30] This is the case whether the firm is solvent or insolvent. By contrast, where the firm is of fixed duration, it cannot be dissolved by the mere giving of notice by one partner to the other partners. The partner's creditors cannot compel the partner to exit from the firm and force a pay-out from the firm's assets. Scottish firms of fixed duration therefore exhibit strong entity shielding, whereas partnerships at will exhibit weak entity shielding. Kraakman et al's conclusion that *all* partnerships show weak entity shielding does not accurately describe Scottish partnerships.

Kraakman et al's second attribute was, in essence, agency doctrine. The Scottish firm operates through partners as agents. Although enshrined in s.5 of the UK Partnership Act 1890, the partner's status as agent pre-dates that Act considerably, expressed for example

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[25] J B Miller, *Partnership Law in Scotland*, 2nd edn, (1994) 591.
[26] Ibid.
[27] See also D Cabrelli, (2010) JCLS 343 at 350-351, and ss39 and 44 Partnership Act 1890. On the nature of the partner's share as an incorporeal moveable right, see G Gretton "Who owns partnership property?" (1987) Jur Rev 163 at 165, who cites Bell, *Commentaries,* II,536.
[28] The Laws of Scotland: Stair Memorial Encyclopaedia, Diligence, vol 8, paras 115 and 116.
[29] Partnership Act 1890, s32(c).
[30] Partnership Act 1890, s.26(1) and see also the rule in *Moss v Elphick* [1910] 1 KB 846, which applies in Scotland.

in 1751 by the institutional writer, Bankton (although not, of course, using the language of modern agency).[31]

Kraakman et al's third attribute was suing in appellation. The Scottish rules on this issue are complex. A distinction is made in the Court of Session (the highest court for civil matters located in Scotland)[32] but not in the sheriff court between using a social name (e.g. Richardson, Cabrelli and Partners) and using a descriptive name (e.g. The Ayrshire Transport Company).[33] In the Court of Session, where the firm uses a social name, whether the names are or are not the names of the present partners, the firm may sue or be sued in the firm name alone.[34] A firm with a descriptive name must add, in addition to that descriptive name, the names of three of the partners or all of the partners if less than three.[35] In the sheriff court whether the firm uses a social name or a descriptive name, the firm may sue and be sued in that name.[36] Thus not every Scottish firm has the ability to sue in its firm name alone in the Court of Session.

In this Section One the application of Kraakman et al's framework to Scots law has highlighted the inchoate nature of the Scottish firm's legal personality. Although able to contract or own assets in its own name, it often does not do so. Its ability to sue in

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[31] Andrew McDouall, Lord Bankton, *An Institute of the Law of Scotland,* (1751), reprinted 1993, I,22,6: "…the deeds of any one of the partners affect the whole, in matters relating to the company [partnership], or where he is manager for them, and acts in their name; because it is understood that they tacitly empower each other to contract for the company, either in disposing of their effects, or purchasing from others…."

[32] The final court of appeal for civil matters in Scots law is the UK Supreme Court, located in London.

[33] Bell, *Principles,* s. 357; F Clark, *A Treatise on the Law of Partnership and Joint-Stock Companies According to the Law of Scotland*, (1866), vol 1, 538.

[34] *Forsyth v Hare* (1834) 13 S 42; Ae J G Mackay, *Manual of Practice in the Court of Session,* (1893), 159; Bell, *Principles,* s. 357, citing *Douglas Hume and Co* June 16 1792 House of Lords Dec 24 1795; *Thomson v Lidell* July 2, 1812, FC; *Campbell v Baird* Feb 13 1827, 5 S D 335; *Forsyth v Hare & Co* (1834) 13 S 42; *Wilson* Jan 20 1836, 14 S D 262; *Thomson* Nov 30 1836 15 S D 173.

[35] *Antermony Coal v Wingate* (1866) 4 M 1017; Ae J G Mackay, *Manual of Practice in the Court of Session,* (1893), p.158; D Maxwell, *The Practice of the Court of Session,* (1980), 143. Bell, *Principles,* s. 357, citing *Culcreuch Cotton Co v Mathie* (1822) 2 S 47; *Scott* Feb 23 1827, 5 SD 414; *Commercial Bank* 28 July 1828, 3 W S 365; *May* Nov 27 1834, 13 SD 94.

[36] Ord Cause Rules 1993, rule 5.7, T Welsh QC, *MacPhail's Sheriff Court Practice*, (3rd edn, 2006), paras 4.94 - 4.96.

appellation is not always obvious. This explains the qualified manner in which it has been discussed: Clarke's "quasi persona";[37] or Gretton's "imperfect" personality.[38]

Beyond the Scottish arena, this Section leads us to reflect on the way one ought to use Kraakman et al's framework. Their list of attributes should not be used in a 'tick box' manner. Attributes may exist in theory but only in weak form in practice. One must look behind the label to the reality of the legal system's recognition of the ability to act in group-form. What may lie beneath the Scottish partnership's inchoate nature is concern over the lack of continuity, an issue considered in Section 1(D), immediately below.

D. Continuity

Legal personality involves giving to the firm an identity distinct from those of the individuals behind it. Distinguishing between identities is important for the ongoing validity of the firm's contracts with third parties. If the contract binds the firm (as distinct from the partners), then a change in the membership of partners will have no effect on the enforceability of that contract. If, by contrast, a change in the membership of partners acts to extinguish the firm, the firm, as a contracting party, no longer exists. Remedies against that firm are unlikely to be successful (although the ex-partners of the ex-firm continue to be personally liable). Although the third party could seek to conclude a new contract with a successor firm, there is no guarantee that the new firm would comply. There may also be concerns over the ownership of assets. Whilst the old firm may have been asset-rich, those assets working to bond its contractual relations, title to those assets may not have been transferred from the old to the new firm. This is, in essence, the problem which currently affects Scottish general and limited partnerships. Limited liability partnerships, constituted in the UK legislation as "bodies corporate", may not suffer the same continuity problem.[39]

Kraakman et al view the firm as a single contracting party or "nexus for contracts". Entity shielding is necessary to bond those contracts and provide third parties with comfort that the firm's obligations will be met. All of this would be placed in jeopardy if, with each

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[37] F Clark, *A Treatise on the Law of Partnership and Joint-Stock Companies According to the Law of Scotland*, (1866), vol 1, 31.

[38] G Gretton, 'Who owns partnership property?' (1987) Jur Rev 163 at 167.

[39] Limited Liability Partnership Act 2000, s1(2) c. We cannot be entirely certain on this point – the issue has not been tested in the Scottish courts.

change in membership, the firm was, practically speaking, extinguished. This problem is all the more acute if we consider that firms, as aggregations of persons gathered for a common purpose, seem eminently likely to enter into long-term "relational-type" contracts.[40]

It comes as a surprise, therefore, that continuity, or perpetual succession, is not included in Kraakman et al's list of the attributes common to business forms possessing legal personality. Elsewhere, they suggest that perpetual succession may be inappropriate in a business form in which the identity of the individual owners is critical because each is a presumptive firm agent.[41] To them the lack of continuity is not a serious problem, but rather one of a number of rules which are "inconveniences for a smoothly running firm", which can be "avoided by contractual means".[42] Other commentators differ, seeing perpetual succession as part of legal personality.[43] Indeed, lack of continuity is often seen as a factor pointing against legal personality.[44] Kraakman et al's identification of contractual workarounds as a solution is puzzling given that, in the common law, the burden of liabilities is not easily transferred. Section 3 below illustrates this point in relation to Scots law.

At the root of the Scottish continuity problem is adherence to *delectus personae*. To recap, this dictates that the choice of each individual partner implies the exclusion of others.[45] Emphasis of *delectus personae* in Roman law[46] caused the Roman partnership to

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[40] Although the idea of a "relational contract" most famously developed in the work of Iain R. Macneil, the current author uses the phrase to describe the concept developed recently in judgments of Lord Justice Leggatt in the English Courts (*Yam Seng Pte Ltd v International Trade Corp Ltd* [2013] EWHC 111 (QB); [2013] 1 All ER (Comm) 1321).

[41] Hansmann, Kraakman and Reiner, 1394.

[42] Hansmann and Kraakman, 413, a view repeated in Hansmann, Kraakman and Squire, 1394.

[43] M Welters, 'Towards a Singularity of Legal Personality' (2013) 92 Canadian Bar Rev 417 at 417-419, 423 and 455.

[44] A fact noted by Hansmann and Kraakman at 412-413. To Hemphill its absence is a "piece of evidence against the legal personality of the firm", 'The Personality of the Partnership in Scotland' (1994) Jur Rev 208 at 240.

[45] W W McBryde, *The Law of Contract in Scotland,* (2009, 3rd edn) para 12-36. Although Stair does not use the phrase '*delectus personae'* in his discussion of society, he nevertheless emphasises that consent is the basis of society, and that society is "finished" on the death or incapacity of one of the partners, Inst I.16.5. See also Bankton, Inst, I.22.18. Erskine uses the phrase '*delectus personae*' to explain these issues, Inst, III.3.22.k.

[46] A M Fleckner, "Roman Business Associations" in G Dari-Mattiacci and D Kehoe (eds) *Roman Law and Economics*, (forthcoming) (2019) 19.

suffer from a lack of continuity.[47] Although rendering it "rather vulnerable and inherently unstable" these effects were tempered by, for example, the use of extended family members as partners.[48] The lack of stability followed a certain logic because Roman partnerships were essentially designed to be temporary arrangements.[49] The emphasis of personal relationships, appropriate in Roman law, is inappropriate for modern Scots law where the number of partners is, with certain exceptions, unlimited, and where partnerships operate on a global scale. Having failed to progress from its Roman origins, the problem for Scots law is more than a "mere inconvenience". As we shall see in Section 3, the contractual workarounds which have been developed have been largely unsuccessful.

E. "Owner shielding"

To Hansmann and Kraakman, entity shielding is not only an attribute of legal personality, but the "defining characteristic of a legal entity".[50] It is the one attribute which cannot be achieved through contract alone.[51] To recap, entity shielding protects the firm's assets from claims of the personal creditors of the owners of the entity. Owner shielding is the mirror image of entity shielding: the protection of the owners' personal assets from claims by the firm's creditors. In the corporate context, this is, in essence, limited liability.[52] To Hansmann and Kraakman, entity shielding is much more important than limited liability:[53] whilst firms can prosper without limited liability, enterprises lacking entity shielding are "largely unknown in modern times".[54]

Owner shielding is *not* generally treated as part of legal personality. It can, however, be difficult to separate the two: in common thought limited liability can be perceived as a way in which the owners of a company can distance their personal assets from the claims of

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[47] B Abatino, G Dari-Mattiaci and E Perotti, "Depersonlization of Business In Ancient Rome" 31 (2011) OJLS 365 at 368.
[48] Wim Broekaert, "Joining Forces. Commercial Partnerships or Societates in the Early Roman Empire" 61 Historia 221 at 229.
[49] Ibid, although he notes the existence of certain *societates* with a long duration.
[50] Hansmann and Kraakman, 390. In this context, they refer to it as "affirmative asset partitioning".
[51] Hansman and Kraakman, 440.
[52] Kraakman et al analyse limited liability in the section which immediately succeeds the section on legal personality, 8-11.
[53] Hansmann and Kraakman, 390.
[54] Hansmann, Kraakman and Squire, 1336.

the company's creditors. It is such an important piece of the jigsaw puzzle that it is explained here in relation to Scots law.

The Scottish partnership has a distinct pool of assets owned by the firm in the firm's name. The partners are not entirely shielded from firm debt, however. The firm is primarily liable for firm debts, partners having a secondary accessory[55] liability resembling the liability of a guarantor (or to use the Scottish word, a cautioner).[56] A debt must be constituted against the firm first of all.[57] In partnerships governed by the Partnership Act 1890, after decree has been obtained against the firm, if the firm has failed to pay that debt, that decree may be enforced against any one of the partners in full, through the operation of joint and several liability.[58] A partner who has paid the whole or part of the firm debt may recoup a share of that debt from the other partners equally, or in the shares set out in the partnership agreement.[59] This scheme changes in the case of limited partnerships (where only the general partner is personally liable for firm debts) and for limited liability partnerships (where no member is personally liable for LLP debts). Despite the pattern of primary and secondary liability existing in partnerships governed by the 1890 Act, it is common in practice to sue the firm *and* the partners individually in the same court action.[60]

Looking at the impact of partnership debt on the partners' creditors, those personal creditors have no priority over partnership creditors in relation to the partner's individual

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[55] R Anderson, "Juristic Persons" in Iain G MacNeil (ed), *Scots Commercial Law* (2014) 5.
[56] *Mair v Wood* 1948 SC 83, per Lord President Cooper at 86; *Neilson v Wilson* (1890) 17R 608 per Lord President Inglis at 612; J J Gow, *The Mercantile and Industrial Law of Scotland* (1964) 545. Once it is understood that "caution" is the Scots word for guarantee, readers will understand the pun in the title of this article.
[57] Ae J G Mackay, *Manual of Practice in the Court of Session,* (1893), 172.
[58] F Clark, *A Treatise on the Law of Partnership and Joint-Stock Companies According to the Law of Scotland*, (1866), vol 1, 285; Ae J G Mackay, *Manual of Practice in the Court of Session,* (1893), 172. Partnership Act 1890, s. 9. This section applies *joint* liability to English partners and *joint and several* liability to Scottish partners. Restrictions of space prevent discussion of the full repercussions of this difference here. For joint liability in Scots law, see Erskine's Inst 3,3,74 (1st edn, 1773); Bell's Prin ss 51-62 (4th edn, 1839); W W McBryde, *The Law of Contract in Scotland*, (3rd edn, 2007), chap 11. For joint liability in English law see E Peel, *Treitel's Law of Contract,* (14th edn, 2015), para 13-005. For several liability in both systems see *Wilson on Debt,* (2nd edn) para 28.1 and D Sellar, '"Several" Problems for Banking Lawyers' 1993 JBL 80. For joint and several liability in Scots law see Erskine's Inst 3,3,74 (1st edn, 1773); Bell's Prin ss 51-62 (4th edn, 1839).
[59] Partnership Act 1890, s. 24(1).
[60] S Chan, *A Practical Guide to Partnership Law in Scotland* (2018) para 4-02.

assets. In other words, Scots law has not applied this part of the "jingle rule" historically applied by English law.[61]

Returning to Hansmann and Kraakman, the Scottish firm does not display the complete owner shielding displayed by the limited company. Complete owner shielding, it will be recalled, fully severs the claims of firm creditors from the personal assets of owners.[62] This is not the case in the Scottish firm: whilst the firm is primarily liable for firm debts, individual partners have a secondary liability, engaged if the firm has insufficient capital to cover firm debts. Nor does the Scottish firm display the type of weak owner shielding which they identify. Personal creditors do not have priority over firm creditors in the division of the partners' personal assets.[63]

Section 2. Historical Development of Separate Legal Personality in Scots Law

This Section explores the historical development of separate legal personality of the Scottish firm, from the early Roman-inspired contract of *societas*, largely centred on the internal rights and duties of the partners *inter* se, to the development of a modern business vehicle in the late eighteenth and early nineteenth centuries. It is in this latter period that legal personality, a key issue in understanding the way in which contracts with the firm are enforced, and the way in which the firm's assets bond those contracts, emerged.

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[61] This rule dictates that "…the joint creditors of a partnership cannot access individual assets of the partners until the partnership funds are exhausted; and the individual creditors of individual partners cannot access other partners' assets until the person assets of the partner (including his share of the partnership capital) is exhausted", Joshua Getzler and Mike Macnair, "The Firm as an Entity Before the Companies Acts" in Paul Brand, Kevin Costello and W N Osborough (eds), *Adventures of the Law, Proceedings of the Sixteenth British Legal History Conference 2003* (2005) 267 at 278. The word 'jingle' describes the fact that it is easy to remember: "Partnership estate to partnership creditors, private estate to private creditors, anything left over from either go to the other". See also J J Henning, "The Dual Priorities Rule and the Insolvent Partnerships Order of 1994" (2010) 31(5) Company Lawyer 131.

[62] Hansmann, Kraakman and Squire, 1340.

[63] Hansmann, Kraakman and Squire, 1339.

A. Roman law and the early institutional writers

Societas, one of the consensual contracts in classical Roman law, was "…not a corporate body, a legal person in its own right".[64] In marked contrast with Hansmann and Kraakman's conception of the firm, the focus lay on the rights and duties of the partners *inter se*,[65] and the allocation of the economic benefits of the partnership's business activities internally amongst the partners. Agency, or the ability of managers to bind the firm (Kraakman et al's second attribute) was also lacking. A partner could not bind the *societas* in contracts with third parties.[66] Any contract formed by a partner with a third party could only bind the partner as an individual. The underlying reason for this position lies in the Roman attitude to agency rather than partnership:[67] it lacked any idea of direct representation which would have allowed a partner to bind the partnership in legal relations with the outside world.[68] Instead, a number of other concepts were used to achieve similar results, for example, the ability of a *paterfamilias* at the head of a Roman family to operate in business through sons and slaves.[69] Finally, both elements of entity shielding were lacking: there was no distinction between the obligations and assets of the *societas* and those of its members.[70]

Roman law recognised "non-human right and duty-bearing entities".[71] Known as *corpus* or *universitas*, they were treated in many respects like persons even though they were not persons.[72] *Universitas* to the Roman jurists was "a group which has been recognised by the law to be a group and either made capable or recognised to be capable as such of rights and duties".[73] The *universitas personarum* was considered as a person, or a corporation in Roman law. It had legal capacity and the ability to change with changes of

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[64] R Zimmermann, *The Law of Obligations Roman Foundations of the Civilian Tradition* (1996) 455

[65] J A C Thomas, *Textbook of Roman Law,* (1976) 302; P Stein, 'The Mutual Agency of Partners in the Civil Law' (1958-1959) Tul L Rev 595 at 595.

[66] J A C Thomas, *Textbook of Roman Law,* (1976) 302.

[67] Stein, 'Mutual Agency' 596.

[68] R Zimmermann, *The Law of Obligations Roman Foundations of the Civilian Tradition* (1996) 413-418.

[69] W M Gordon, 'Agency and Roman Law" in *Roman Law, Scots Law and Legal History*, (2007) pp. 342-343; R Powell, 'Contractual Agency in Roman Law and English Law' 1956 S A L Rev 41.

[70] W W Buckland, *A Textbook of Roman Law* (1921) 504-7.

[71] J A C Thomas, *Textbook of Roman Law* 387

[72] Ibid.

[73] P W Duff, *Personality in Roman Private Law* (1938) 37.

membership.[74] Pope Innocent IV is thought to have developed the idea of the *universitas* as a person at law in the mid thirteenth century.[75]

In her analysis of the corporation in Western Christendom, Reynolds concluded that until 1300, there was no room for a doctrine of legal persons.[76] She argued that, before this time, collective nouns such as *universitas, communitas* and *collegium* were used so widely as to show that they had no connotation at law.[77] It was only after 1300 in England that the first charters of incorporation were created as a response to legislation on mortmain, and that this created the circumstances in which lawyers could begin to conceptualise legal personality.[78] Hunter, in his work on the personality of the Scottish burgh, emphasised the entirely separate development of English and Scots law, and the "late" development of ideas of personality in Scotland.[79] He suggested that it was only with the development of a Supreme Court for Scotland, and the jurisprudence of that court, that ideas of separate legal personality were considered, and that the Scots lawyer of the time, trained in the civil law, turned to civilian jurisprudence to understand these ideas.[80]

Craig, the first Scottish institutional writer, writing in the late 1590s, accepted both the notion of the corporation and its ability to both give and accept feus of property.[81] Although it is possible that Craig's work influenced the later institutional writers in this respect, there is no direct evidence that this was the case. "Society" (partnership) is covered by the institutional writers of the late seventeenth and eighteenth centuries: Stair, Bankton and Erskine. They discuss *delectus personae*,[82] i.e. the choice by contracting party A of contracting party B because of B's special skill or knowledge which rules out assignment

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[74] See the analysis in A Popovici, 'Quebec's partnership: une société distincte' (2013) J Civ L Stud 339 at 345; G Gretton, 'Trusts without Equity' (2000) 49 ICLQ 599 and in R Valsan (ed), *Trusts and Patrimonies* 87 at 103-104.

[75] Susan Mary Watson, "The Corporate Legal Person" (2019) JCLS 137 at 142.

[76] Reynolds, "The Idea of the Corporation" 31.

[77] Reynolds, "The Idea of the Corporation" 28.

[78] Reynolds, "The Idea of the Corporation" 32-33.

[79] Hunter, "Corporate Personality", particularly at 229, 232, and 234-235.

[80] Hunter, "Corporate Personality" 236-237.

[81] Thomas Craig, *Jus Feudale*, translated and edited by Leslie Dodd, (2017) Book 1, 1.15.16. Although it was published in 1655 it was circulated amongst lawyers in manuscript form before that date. Hunter characterises this as the acceptance of the civilian form of corporation, "Corporate Personality" 237.

[82] For analysis see W W McBryde, *The Law of Contract in Scotland,* (2009, 3rd edn) paras 12-36 – 12-41.

(in Scotland, assignation) or the transfer of rights under the contract. Although they use language suggestive of the partnership as a whole or unified thing,[83] the point being made is that there is only one contract which falls when one partner leaves, rather than a number of individual contracts between partners.

Erskine, writing in 1773, confirmed that rights acquired by a partner in the name of the company, vest in the company [using the word "company" here to mean partnership].[84] He referred to the "company effects" as the "common property of the company".[85] Partners can subscribe deeds on behalf of the firm, binding the firm.[86] Discussing the joint and several liability he stated "all the *socii* [partners] are, in regard to strangers, considered as one person".[87] Hemphill, writing in 1994, concluded that it is only later, in the works of Bell, that we find a developed idea of legal personality.[88] Although he cites Erskine's reference to ownership of assets, he does not cite Erskine's references to subscription of deeds and appearance to "strangers". This author therefore disagrees with Hemphill: in Erskine's work we do indeed see attributes of legal personality emerging.

B. **The Contribution of George Joseph Bell**

The Scottish institutional writer, George Joseph Bell[89] has been credited with creating the separate legal personality of the Scottish partnership.[90] Certainly, Bell may have been the

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[83] Stair stated: "…it is like a sheaf of arrows bound together with one tie, out of which, if one be pulled, the rest will fall out", *Institutions of the Law of Scotland* I,16,5. Bankton explained joint and several liability to third parties by saying "…because the party that contracts with them [the third party] relies on the faith of the company and by the nature of the contract they are united into one" *An Institute of the Laws of Scotland* (1751, reprinted 1993) I,22,6. See to the same effect MacKenzie, *Institutions of the Law of Scotland,* (2nd edn, 1688) 247.
[84] John Erskine, *An Institute of the Law of Scotland* 1st edn, (1773), 3,3,20.
[85] John Erskine, *An Institute of the Law of Scotland* 1st edn, (1773), 3,3,24.
[86] John Erskine, *An Institute of the Law of Scotland* 1st edn, (1773), 3,3,20.
[87] John Erskine, *An Institute of the Law of Scotland* 1st edn, (1773), 3,3,29.
[88] Peter C Hemphill, "The Personality of the Partnership in Scotland" (1994) Jur Rev 208 at 216.
[89] For Bell's life and work, see D M Walker, *The Scottish Jurists* (1985) 337-351 and K G C Reid, "From Text-Book to Book of Authority: The Principles of George Joseph Bell" (2011) 15 EdinLR 6.
[90] Hemphill states: "The only remaining Institutional writer is Bell. Here at last appear statements of the personality of the partnership, expressed in abstract form as general

first to use the conclusory language or label of separate legal personality. Nevertheless, the elements from which Bell constructed personality existed at the end of the eighteenth century, and were recognised by Erskine. This is not to down-grade Bell's role. Crucially, he moved Scots law from a purely contractual, Roman idea of partnership as a contract, towards partnership as a business, able to conclude contracts with third parties and with a separate pool of assets to bond those contracts. In Hansmann and Kraakman terms, Bell engages organisational law to develop the modern Scottish partnership.

This transformation can be observed in successive editions of Bell's *Commentaries*. In the first edition (1800-1804) attributes of legal personality appear early in his treatment.[91] Partnerships are "…. capable under a particular name or firm, of dealing as a separate person, and contracting with others all the relations of debtor and creditor…"[92] The context within which this statement is made is important. Immediately prior to it, Bell focussed on the *contractual* nature of partnership, namely the rights and duties of the partners *inter se*.[93] He then stated: "But when viewed relatively to bankrupt law, we are to dwell less on the rights of the partners, and to consider the interests of the creditors as of chief importance".[94] Given that *Commentaries* evolved from an earlier publication dedicated solely to bankruptcy, this focus is not surprising. Nevertheless, it is important because this focus on bankruptcy encourages him to make the leap from the limited, essentially Roman idea of partnership as a contract, to partnership as a business. Here we see the engagement of organisational law in the manner emphasised by Hansmann and Kraakman.[95]

From the third edition of *Commentaries* onwards, treatment of legal personality, although appearing later, is more pronounced, occupying a section in its own right, either fourth or fifth in the overall treatment.[96] It has become controversial: "[s]ome lawyers have

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principles" 216, reaching this conclusion after a short discussion of the relevant passage of the 7th edition of *Commentaries.*

[91] *Commentaries*, (1st edn, 1800-1804), vol 2, 495. This is the Introduction to Book VIII, Partnership.

[92] *Commentaries*, (1st edn, 1800-1804), vol 2, 495.

[93] Quoting Pothier's *Traité du Contrat de Société*, vol 2, 533, from which Bell draws a definition of the contract of partnership.

[94] *Commentaries*, (1st edn, 1800-1804), vol 2, 495 (**check).**

[95] Hansmann and Kraakman, 387.

[96] See for example *Commentaries*, (3rd edn), vol II, 510.

considered the obligation of the company [partnership] only as the joint and several obligation of the partners. But this is not correct".[97] Writing at a time of extensive English influence on Scots law, he may have been reacting to those who sought to assimilate Scots with English law.

In the third edition, for the first time, he cites a case as an authority for legal personality: *A v B* from 1741.[98] In that case, Lord Kilkerran stated: "[t]he creditor of a company cannot pursue one of the partners for a company debt: his action lies against the company only".[99] Thus, Bell's discussion of legal personality in his first two editions proceeded *without* reference to a Scottish case, a relevant case being added only in the third edition. Given that the case predates the first edition by more than 50 years, one wonders whether Bell was slow to notice it.[100]

In the fourth edition (1821), reference to the controversy has disappeared, and Bell has begun to explore the differences between Scots and English law. In England there can be no debt between two partnerships in each of which one person is a partner, whereas in Scotland this is possible.[101] By the fifth edition (1826, the last published during his lifetime) the controversy has returned.[102] Bell spends more time setting out the various manifestations of separate personality, for example, the ability to sue in appellation.[103] His tone remains slightly defensive of the existence of legal personality.

Bell's other well-known work, *Principles* (a book intended for students) adopts the classic approach of a textbook, first asserting the general principle, before listing manifestations:

> "The company [partnership] forms a separate person, 1. competent to maintain its relations with third parties by its separate name or firm, independently of the

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[97] *Commentaries*, (3rd edn), vol II, 510.
[98] Kilkerran 26 Feb 1741. Kilk 518. Also reported (1741) Mor 14,560.
[99] 26 Feb 1741, Kilk 518. Also reported (1741) Mor 14,560.
[100] Interestingly, Bell also appears to have missed the Arran Fishing Company case, *John Stevenson and Co v McNair and Others* (1757) Mor 14,560, discussed below, adding it only in his fourth edition, see Ross Anderson, "Partnership" in Iain G MacNeil (ed) *Scots Commercial Law* (2014) 135 at 136, fn 7.
[101] *Commentaries*, (4th edn), vol II, 620.
[102] *Commentaries*, (5th edn), vol II, 619.
[103] The partnership's ability in this respect is supported by reference to one case, *Calcreuch Cotton Co* 27 November 1822 2 Shaw and Dunlop 47.

> partners; 2. capable also of holding a lease, but not of holding feudally as a vassal; 3. a company having a firm name may sue or be sued by it; 4. a company having only a descriptive name can appear judicially only by or with some of all of the individual names".[104]

Scottish cases from the early nineteenth century are cited as authorities for propositions 2. to 4., but no authority is given for proposition 1. No other sources are cited.

In conclusion, the author suggests, contrary to Hemphill, that attributes of legal personality were forming in the late eighteenth century. Bell assembled these attributes and developed them into a more comprehensive idea. We do not know why, but he expressed his ideas first, adding an older case to support them much later. We now turn to Scottish case law contemporaneous with Bell's works to investigate whether that case law sheds light on these issues.

C. Eighteenth Century Case Law

In this Section 2(C) the author discusses case reports contained in Morison's Dictionary, spanning the late seventeenth to the early nineteenth century. This section, extending to sixty-six pages and a nineteen-page appendix, has been largely overlooked by Scottish scholars. *A v B* from 1741, the case relied on by Bell, is indeed, the earliest case to refer to separate legal personality. A case decided in 1757 concerning the partners of the Arran Fishing Company,[105] is notable because of counsel for the defender's citation of Jacques Savary's *Le Parfait Negociant*,[106] to support his argument that his client was not personally liable for partnership debts. His client was ultimately successful although on other grounds.

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[104] *Principles,* (4th edn, 1839), s. 357.

[105] *John Stevenson and Co v McNair and Others* (1757) Mor 14,560.

[106] *Le Parfait Negociant, ou instruction générale pour ce qui regarde le commerce de toute sorte de marchandises de France et des pays étrangers, Second partie* L. 1. C. 1. 24. The section of the book quoted relates to the French *Société en Commandit*é or limited partnership. Jacques Savary (1622-1690) was a successful businessman who served on a commission advising the French Government on revising the laws governing trade and commerce. Le Parfait Negociant grew from the memoirs he prepared whilst advising the commission (see Morgan Witzel, *A History of Management Thought*, 2nd edn, (2017) 94). First published in 1675, the eighth edition of this book (1721-1724) was purchased by the Advocate's Library in 1730. It seems likely that it was this edition that counsel relied on in this case.

The case has been interpreted as an (ultimately unsuccessful) attempt to introduce the French *société en commandité* or limited partnership into Scots law.[107]

From this point onwards, judging from the case reports, advocates were both familiar with, and using, the concept of separate legal personality in Scottish partnership litigation. Savary's *Le Parfait Negociant*[108] is relied on in a further case decided in 1766.[109] Counsel's submissions resemble a list of the manifestations of legal personality:

> "Persons united in a proper copartnery are liable *singuli in solidum,* and bound by the actings of the different partners. With respect to the trade in which they are engaged they act as one person, subscribe by one name, and transact business in one house, from which, and other circumstances, the public are induced to deal with each partner on the credit of the whole".[110]

In 1774, successful counsel in an Inner House case stated:

> "..a trading society is a distinct *nomen juris*, and having different qualities and rights from the individuals composing it, there can be no doubt. The distinction between a company [meaning here a partnership] and the individuals goes through every species of transaction."[111]

Despite the fact that this case was heard the year after publication of Erskine's *Institute,* the failure to refer to that work is not surprising: Erskine's ideas will have taken time to gain currency.

In 1796, in two separate hearings of a case, counsel made a direct link between Scots law and the Roman concept of a *universitas*:

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[107] J Robertson Christie, "Joint Stock Enterprises in Scotland before the Companies Act" (1909) 21 Jur Rev 128; Anderson, "Partnership" 136. The case was not followed in *Douglas Heron & Co v Hair* (1778) Mor 14,605. The Limited Partnership was introduced into the UK as a whole by the Limited Partnership Act 1907.
[108] Book 1, chap 1.
[109] *Donaldson v Paul and Ors* (1766) Mor 14,609
[110] Ibid. The comments were made in order to distinguish a partnership from a joint venture.
[111] *Galdie v Gray* (1774) Mor 14,598 at 14,599.

> "The creditors of a Company [meaning partnership] are preferred on its funds, because the stock of the company is, in law, held to belong not to the partners, but to the Company, considered as a *universitas*, against which the partners, and consequently their private creditors in their right, have a *jus crediti*, only for the residue after payment of the debts of the Company".[112]

Erskine's view on ownership of property (quoted above) is relied on.[113] Counsel's statement is redolent of Hansmann and Kraakman's asset-partitioning: the assets are owned by the partnership as a separate legal person, not by the partners collectively as individuals. In the second hearing counsel stated: "…a company is, in law, considered as a *universitas* or corporation, distinct from the partners who compose it…"[114]

In the cases discussed above, no single advocate appears twice. Although Bell practised at the Scottish bar, he is not amongst the advocates concerned. Whilst the French limited partnership may not have taken root in Scotland, Savary's book was used on a number of occasions to develop the emerging legal personality of the Scottish partnership. The idea of the Roman *universitas* was also used as a useful analogy. References to Roman sources in these cases on issues other than legal personality are common.[115]

In conclusion, the prevailing view, that Bell created the partnership's legal personality, is not entirely accurate. He drew on ideas which had developed in the previous century, in case law and in the works of Erskine. Bell was nevertheless instrumental in developing the Scottish partnership into a fully functioning business, able to exercise ownership over assets and to partition those assets for the bonding of the firm's contracts.

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[112] *Campbell and Ors v Blaikie* (1796) Mor 14,611. Authority for this proposition is taken from the Digest (L. 27. D. Pro. Socio) and Erskine, 3,3,24.
[113] Erskine, *Institute,* 3,3,24 and see above note x.
[114] *Campbell and Ors v Blaikie* (1796) Mor 14,612 at 14,613.
[115] *Fairholm v Marjoribanks* (1725) Mor 14,558; *Aiton and Co v Cheap and Ors* (1769) Mor 14,573; *Campbell and Ors v Blaikie* (1796) Mor 14,612; *Warner and his Curators v Cunninghame* (1798) Mor 14,603.

D. Nineteenth Century Development

In the first major Scottish treatise dedicated to partnership law (or, more accurately, to partnership and company law), published in 1866, F W Clark referred to the "quasi persona",[116] which was nevertheless a "distinctive or central feature of the Scottish partnership".[117] He suggested that legal personality was fully established during the 17th and early 18th centuries,[118] and characterised Scottish partnership law as being based on the principles of the Roman law of *societas*, modified by Dutch and French influences.[119] These claims are unproven in his work: no authority is cited, and he makes no attempt to identify particular sources or influences. Contemporary developments, namely the development of the limited company, may have made it easier for Clark to attach generalised significance to certain features of partnership law.

Clark's views on both the date of development of separate legal personality and its French and Dutch antecedents exerted a significant influence on twentieth century authors,[120] and remains a significant point of reference in the leading modern text.[121]

The nineteenth century ended with the enactment for the UK as a whole of the Partnership Act 1890. The Partnership Bill, drafted by Frederick Pollock, was originally intended to apply to England and Wales only. It was only during the final stages of the Bill's progress through Parliament that the decision was made to apply it to Scotland in addition.[122] Reservations over this course of action were expressed in both the Commons and Lords Committees because of the possibility that it could change, rather than restate, the law.[123] Pollock, the drafter of the Act, was (of course) aware that Scottish partnerships

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[116] F Clark, *A Treatise on the Law of Partnership and Joint-Stock Companies According to the Law of Scotland*, (1866), vol 1, 31.
[117] Ibid.
[118] Clark, *Treatise* 2.
[119] Clark, *Treatise* 2.
[120] For example, T B Smith, *Short Commentary on the Law of Scotland,* (1962) 275-276. J J Gow made no attempt to tackle its origins: see *The Mercantile and Industrial Laws of Scotland* (1964) 544-545.
[121] J B Miller's *Scottish Partnership Law,* second edition by Gordon Brough, (1994) 14-16.
[122] A Rodger, 'The Codification of Commercial Law in Victorian Britain' (1992) 108 LQR 570 at 578.
[123] Hansard, Commons Sitting, HC Deb 10 July 1852, vol 271, cc 2058-61; Hansard Partnership Bill (Lords) No 373, HC Deb, 18 July 1890, vol 347, cc 227-8. I am grateful to Chloe Kennedy, LLB Hons Student, Edinburgh University, 2017, for finding these references.

have separate legal personality.[124] The 1890 Act places the legal personality of the Scottish firm on a statutory footing, section 4, entitled "Meaning of firm", applying an extra sub-section to Scotland only:

> "[i]n Scotland a firm is a legal person distinct from the partners of whom it is composed, but an individual partner may be charged on a decree or diligence directed against the firm, and on payment of the debts is entitled to relief pro rata from the firm and its other members".[125]

3. Continuity

A The Problem Defined

In theory at least, in Scots law each time a partner retires from the firm or a new partner is assumed into the firm, a new firm is created with a new legal personality. This follows from the application of the (Roman) doctrine of *delectus personae* to partnership contracts.[126] Although Erskine described society as "permanent", this is not reflected in case law.[127] This situation undermines the ability of third parties to rely on contracts with the firm and appears to provide firms with an easy escape route from their debts. From a Scottish perspective, this is more than an "inconvenience".[128] One of the major contributions of organisational law is the partitioning of assets to bond firm contracts. Lack of continuity undermines this important function. Changes in membership destroy that bonding effect: assets may be locked in a former emanation of the firm and unavailable to bond the new

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[124] In *A Digest of the Law of Partnership* (2nd edn, 1880, at 19) he stated: "In Scotland…. the firm is a "separate person:" not only can it sue and be sued in the "social name," but it may sue and be sued by its own members, and firms having one or more members in common may sue each other", citing as authorities Bell, *Principles,* s 357 and Second Report of the Mercantile Law Commission, 18, 141.

[125] Hemphill is correct when he suggests that "and its other members" in the last line should be superfluous in a legal system where the partnership has separate personality, (211). Section 5 (on agency) shows similar confusion, see Laura Macgregor, "The Role of Agency in Scottish Partnerships" in Andrew J M Steven, Ross G Anderson and John MacLeod, *Nothing So Practical as a Good Theory*. Festschrift for George L Gretton, (2017), 88 at 89.

[126] Bankton stated that society is dissolved "…at the pleasure of either party", Inst, I.22.19. See also Partnership Act 1890, s 32(c).

[127] John Erskine, *An Institute of the Law of Scotland* 1st edn, (1773), 3,3,20.

[128] Hansmann and Kraakman, 413.

firm's contracts. Lack of continuity causes a number of problems, not all of which can be examined here.[129] Sections 3B and C below analyse contractual workarounds developed by contracting parties and by the Scottish courts. These Sections illustrate that although an entity may incur contractual liabilities wholly or partially separate from its owners, this is no guarantee of efficient bonding of assets to firm liabilities or an efficient capacity to contract with third parties. Perpetual succession is also required.

B Contractual Clauses

Contracting parties may insert a clause into a contract between the partnership and the third party, which indicates that the contract will continue *notwithstanding* any change of partners in the partnership. This clause involves the firm as presently constituted and the third party agreeing to bind the firm howsoever constituted in future, with rights and duties. In Scots law it is possible to confer a *right* on a third party, even where the recipient is not yet in existence.[130] It is not possible to *burden* that third party with duties: novation requires the consent of the third party.[131] In seeking to burden future emanations of the firm with duties, without its consent, the validity of this clause is questionable. The courts have also sought to develop contractual workarounds, considered below.

C Contracts with the "House"

The first example of a judicially created contractual work-around is a line of authority which treats third parties as contracting with the "house". The aim is to confer both rights and duties on the firm *however constituted* from time to time. The Inner House case of *Alexander v Lowson's Trustees*, decided in 1890, is treated as the root of this concept. [132] A partner's trust settlement directed that his estate should, on his death, continue to be vested in the partnership. The daughters of another partner who later died disputed this, arguing that the partnership had been dissolved on the testator's death, and that their

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[129] For analysis of problems caused on dissolution of the firm, see James Bailey, "Phantom Partnerships and Post-Dissolution Profits: *Sheveleu v Drs Brown and Ducker* (2018) 23 EdinLR 230.

[130] Contract (Third Party Rights) (Scotland) Act 2017, s.1(4)(a).

[131] McBryde, *Contract,* paras 25-21 – 25-28.

[132] (1890) 17 R 571.

father's share had become payable to them at that point. Lord Young, in a rather opaque statement, accepts in principle that the contract continues notwithstanding changes in the firm membership.[133] The Inner House emphasised that the business carried out was "practically the same business".[134] Applying this principle to the facts, the testator's wishes were upheld. Lord Young was, however, at pains to limit the court's task to interpretation of the particular deed. The case provides only weak authority for the idea of contracts with the "house".

In the case the defenders had relied on the following passage from Bell's *Commentaries*:

> "The intention of the parties will be studied in the decision of such cases, where the obligation is undertaken to a firm; whether it was meant to be limited to the *partners* at the time, or to be extended to the *house* under all the changes it might undergo".[135]

Although Bell relies on two English cases to support this view,[136] the concept does not appear to have formed part of English law.[137]

In 1971 in a Scottish appeal to the House of Lords the respondents relied on the same passage from Bell.[138] The House held that the death of a partner terminated the lease of a farm to a partnership of which he was a partner.[139] By 1974, Lord Maxwell in the Outer House asserted with confidence that : "[t]he concept of a contract with a "house" is part of our law".[140] Quoting Bell, he characterised the question as essentially one of construction of

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[133] (1890) 17 R 571 at 579. The Lord Justice-Clerk, Sir John Macdonald, and Lord Rutherford concurred.
[134] (1890) 17 R 571 at 579.
[135] 5th edn, (1826), Vol II, 526-527.
[136] *Strange v Lee* 3 East 484; *Barclay v Lucas* I Term Rep 291. The latter is a decision from Lord Mansfield.
[137] As is noted by the Law Commission and Scottish Law Commission, Partnership Law, Consultation Paper No 159, Discussion Paper No 111, para 4.41, note 35.
[138] This time from the 7th edn, (1870), Vol II, 526. This edition, published after Bell's death, was largely a re-publication of the 5th edition, with notes from the editor, John McLaren.
[139] 1971 SC (HL) 1.
[140] *Jardine-Paterson v Fraser* 1974 SLT 93 at 97.

contract.[141] This contract, rather than the partnership contract, is the point of reference, given that the third party may have no knowledge of the terms of the latter.[142]

Contracts with the house share the same fundamental problem as clauses used by the contracting parties: it is not possible in Scots law to burden a party with obligations without that party's consent. The Law Commissions described the conceptual basis of the concept as "not clear",[143] concluding that it should "develop or wither…without statutory intervention".[144]

C. Partners' Liability for Partnership Debts

The case reports contain many examples of disputes in which partners seek to avoid liability for a firm debt because that debt dates from a time when they were not partners. The bedrock of these arguments is the change of legal personality of the firm with the change of partners. The partner argues that she should not be liable for debts incurred by the firm *before* she became a partner. Although the firm name may remain unchanged after her assumption, the new firm has different partners and is therefore a different legal person from the old firm. Nor should she be liable for firm debts after she has retired from the firm. Again, despite having the same name both before and after her retiral, the firm after her retiral has different partners and is therefore a different legal person from the old firm.

Section 17 of the 1890 Act essentially follows this logic, providing that a person admitted as a partner into an existing firm does not thereby become liable to the creditors of the firm for anything done before he became a partner. Section 17(2) provides that a partner who retires from a firm does not thereby cease to be liable for the partnership debts or obligations incurred before his retirement. These sections are opaque – they do not really tell us when a partner can be liable for firm debts. The answer to this question lies in case law.

In order to address this problem, the courts have applied a presumption that, where a new firm takes on the whole assets, stock and business of an old firm, it also takes on the

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[141] 1974 SLT 93 at 97.
[142] Ibid.
[143] Partnership Law, A Joint Consultation Paper, (Law Com No 159, SLC DP No 111) (2000), para 4.41.
[144] Ibid, para 4.42.

whole liabilities of the old firm.[145] A new partner, because she is part of the new firm, becomes jointly and severally liable for the debts of the old firm. The presumption is factual in nature and can be rebutted where the new partner pays a large sum of capital into the firm on her assumption.[146] This could indicate that the firm is not continuing as before. Parties tend to amend this position in partnership contracts, using a clause which expressly states that the new firm is not taking on the debts of the old one. If the facts are consistent with that position, the only way in which the new firm can be liable for the debts is by granting an express undertaking to the creditor of the old firm, or dealings from which this can be inferred.[147]

More recently, Lord Hodge, sitting in the Outer House, developed this approach. He identified the important question as whether the facts gave rise to an inference that the new firm (including the new partner) has assumed the liabilities of the old firm.[148] The presumption comes into play only if substantially the same business is carried on without interruption. It does not apply where the new firm has given value for the transfer (in such a case there are assets in the old firm to meet a creditor's claim and therefore no need for the presumption).[149] Lord Hodge confirmed that where a substantial capital contribution is made by a new partner that *may* be a factor which would tend to displace the presumption.[150] Other factors are relevant: inter alia whether there are outward changes in the business on its transfer from the old to the new firm, the subsequent behaviour of the old and new firms, whether the accounts for the winding up of the old firm are kept separate from the accounts of continuance of the new firm, and the nature of the debt to

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[145] In addition to the cases discussed immediately below, see *McKeand v Laird* (1861) 23 D 846; *Miller v Thorburn* (1861) 23 D 359; *Ocra (Isle of Man) Ltd v Anite Scotland Ltd* 2003 SLT 1232.

[146] *Heddle's Exx v Marwick & Houston's Trustee* (1888) 15 R 698 per Lord Shand. The presumption was rebutted in *Thomson & Balfour v Boag & Son* 1936 SC 2, per Lord President Normand at 10; *Miller v MacLeod* 1973 SC 172.

[147] *Stephen's Trustee v Macdougall & Co's Trustee* (1889) 16 R 779.

[148] *Sim v Howat* 2011 [CSOH] 115 at [30]. This idea had already been discussed in the joint Law Commission project in which Lord Hodge was the lead Scottish Commissioner.

[149] 2011 [CSOH] 115 at [31]

[150] 2011 [CSOH] 115 at [31].

the old firm.[151] The terms of the partnership agreement are relevant but not necessarily determinative "…if the reality of the transaction is otherwise".[152]

Although using the language of presumptions, Lord Hodge's analysis rests on a binding unilateral promise,[153] an obligation which is enforceable in Scots law. The new firm makes a *promise* to the contracting party of the old firm to pay the debt of the old firm. In the case, the relatively small size of the new partner's capital contribution was determined more as a custom rather than by reference to the value of the business run by the firm. Taking this and other facts into account, Lord Hodge held that the presumption applied, and the new partnership assumed responsibility for the debts of the old firm.

In 2018 the issue came before the Inner House. [154] The question at issue was whether contingent liability for the payment of contributions to a pension fund had transferred between successive emanations of a law firm. As partners joined and left the firm, seventeen different emanations of the firm had existed. This contrasted with outward appearances, statements on the firm website claiming that the firm had been established for 100 years. The pursuers, three employees of the firm, raised an action against a later incarnation of the firm, arguing that that firm was liable to make payments to remedy a deficit in the pension fund.

Although, broadly, the Inner House affirmed Lord Hodge's approach, two judges cast doubt on whether the fact that the new firm gives value for the assets of the old firm can displace the presumption.[155] A third party, unconnected with the firm, is unlikely to know about such issues.[156] Although their statements are *obiter* (as they both acknowledge), unanimity on this point at Inner House level is unlikely to be ignored in future. Thus, a court should in future take a wholly objective approach to the question whether the new firm has assumed the liabilities of the old firm.

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[151] 2011 [CSOH] 115 at [32].
[152] 2011 [CSOH] 115 at [31].
[153] 2011 [CSOH] 115 at [33].
[154] in *Scottish Pension Fund Trustees Ltd v Marshall Ross & Munro and others* [2018] CSIH 39.
[155] Lord Drummond Young and the Lord President (Carloway).
[156] [2018] CSIH 39 per the Lord President at [48] and Lord Drummond Young at [63] and [71].

Lord Drummond Young characterised the approach as essentially equitable:[157] "…where the new partnership takes over the assets of the old partnership, creditors should not be prejudiced, but should be able to enforce the obligations of the old firm against the new firm".[158] Whilst recognising the conceptual problems inherent in binding future emanations of the firm without their consent, he suggested that consent could be implied, for example, where the third party accepts payment from the new entity or raises proceedings against it for payment of a debt or fulfilment of an obligation.[159] The pursuers' claims passed the test of relevancy, and the case proceeded to proof before answer. Only at this later stage will the court apply the presumption to the facts.

To sum up the existing law, the presumption continues to govern. When it operates, there is continuity. If, on the facts, it does not, there is no continuity. The approach is objective: the third party should not be affected by dealings known only to the partners. The solution, failing to solve the conceptual problems, suffers from the classic defects of judge-made law.

Conclusion

It has been argued here that we should not treat legal personality as a uniform concept. There is "no gradual process of jurisprudential enlightenment"[160] or finish line to the race. Kraakman et al are correct to describe legal personality as a mechanism to bundle a set of legal characteristics or a "convenient heuristic formula".[161] What the Scottish experience underlines is the need to look behind the label, not only to see whether the attributes exist, but also to assess how strong or weak they are in practice.

The historical analysis highlighted the period during which Scots law moved from partnership as a contract impacting only the partners, to partnership as a business vehicle. It has been suggested here, contrary to the prevailing view, that attributes of legal personality emerged from case law from the late eighteenth century and in the works of the institutional writer, Erskine. Of key importance, however, is the role of Bell, whose

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[157] In contrast to English law, Scots law did not experience a separation between courts of law and equity. This word is therefore used in a "non-technical" sense.
[158] [2018] CSIH 39 at [61].
[159] [2018] CSIH 39 at [64].
[160] Hunter, "Corporate Personality" 223.
[161] Kraakman et al, 8.

perspective from bankruptcy law allowed him to develop a comprehensive concept of legal personality in the early nineteenth century. This reflects Hansmann and Kraakman's emphasis of organisational law as the body of rules which allows the firm to contract with third parties, using firm assets to bond those contracts. The article also highlighted two sources which at least contributed to the development of legal personality in Scots law. Both were used in oral submissions in court, in a sense, part of the "living law". Advocates used, firstly, Savary's *Le Parfait Negociant*, and secondly, the Roman idea of a *universitas*. The Scottish experience accords with Hansmann and Kraakman's view that legal personality develops gradually.

Whilst no one would doubt the importance to businesses of Kraakman et al's entity shielding, it is not enough *on its own* to create workable partnerships. Scots law possesses an entity which can incur contractual liabilities separate from those of its owners, and a separate pool of assets to bond those contracts. This has, however, not guaranteed efficient and workable partnerships. Lack of perpetual succession has undermined these important capabilities. Contractual workarounds are unsatisfactory in theory and in practice. Scottish contracting parties continue to take extra measures, such as adding partners in their capacity as trustees as contracting parties. In a legal system which recognises the separate personality of partnerships, this should not be necessary. Law reform is required and should take place at the level of organisational law (through statutory amendment) rather than contract law. As Watson aptly comments: "[n]o amount of contracting though can create a legal person and make it a legal entity separate from human beings…"[162]

A further theme of this article has been the way in which partnership has "outgrown" its personal nature. This justified *delectus personae* in Roman law, and Roman law shaped Scots law in this respect. It is identified by Hansmann and Kraakman as the reason why perpetual succession is "inappropriate" for partnerships. These assumptions are questionable in a modern context. The inappropriate emphasis of personal relationships is a problem which impacts on other parts of partnership law. The time may be ripe to reconsider, for example, good faith duties between partners, or fiduciary duties between partner and firm (in Scots law).

[162] Watson, "The Corporate Legal Person" 140.

Finally, this article has identified some unusual and unexpected results. The Scottish fixed term partnership displays strong entity shielding, running counter to Kraakman et al, who characterise partnerships as exhibiting weak entity shielding. Whether this is an oddity of Scots law or a more general phenomenon shared by other “mixed” legal systems is an issue which remains to be seen.